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Alberta ECONOMIC OUTLOOK

MARCH, 1974

INFLATION 1974

The Financial Post in a recent survey of economic forecasters discovered a range of estimates for inflation during 1974 which varied from 6¾ to 9 percent. It seemed that the only common view was that the rate of inflation would decline towards year end. In an attempt to clarify the issues involved a brief discussion of the factors bearing on the current inflationary situation is set out below.

External Sources

There has been a tendency to blame Canada's inflationary problems on events external to our control. Attention has focussed particularly on a series of "unprecedented events" which triggered an explosion of world commodity prices. The events include the failures of the Peruvian anchovy fishery and the 1972 Soviet grain harvest, the purchase of 25 percent of the 1972 U.S. wheat crop by the U.S.S.R., the coincidence of strong economic expansion in all the main industrial countries and, finally, a drastic escalation of petroleum prices which attended the Arab-Israeli War and the activities of the O.P.E.C.

If one is prepared to dig a little deeper, it becomes apparent that the rapid growth in trade and output which was enjoyed by the western industrial countries from 1971 to 1973 was linked to the huge U.S. balance of payments deficits from 1969 to 1972 which swelled the quantity of U.S. dollars in foreign hands from $15,998 millions to $61,520 millions. In consequence the world's money supply expanded by approximately 92 percent between 1969 and 1972 after having grown by a mere 4.2 percent between 1965 and 1968.

The commodity price boom was also influenced to a large extent by the collapse of the Bretton Woods international monetary agreement. As a hedge against ensuing currency uncertainties speculators turned to the bullion and commodity markets. That a large part of the commodity price boom is due to speculation can readily be appreciated by comparing graphs of the free gold price and **The Economist** index of commodity prices which display a remarkable similarity.

Internal Sources

While no one would disagree with the argument that Canada's inflation is strongly influenced by recent world events, it should be pointed out that the roots of the present Canadian inflation are deeper and closer to home than the preceding analysis would indicate. Inflation in Canada as represented by the C.P.I., accelerated steadily at an annual average 0.54 percentage points a year between 1960 and 1969 to reach a level of 4½ percent. In addition, since mid 1970 onwards the Canadian money supply has been expanding at an annual average rate of about 15 percent. To some extent the authorities were possibly misled by the high rate of unemployment over the period which was at a level which traditionally indicated the existence of economic slack. However, unemployment figures in recent years have been becoming less reliable as an indicator of the pressure of demand on industrial capacity. Unemployment has risen relative to demand pressure so that relative price stability has only been attainable at successively higher levels of unemployment than in the past. The problem is not restricted to Canada; all the other OECD countries are experiencing the same phenomenon.

In Canada it appears that the reasons for this have been a very rapid increase in the labour force, changes in unemployment registration procedures and expansion of unemployment benefits. Professor H. G. Grubel of Simon Fraser University estimates that 2 percentage points of the 1972 unemployment rate of 6.3 percent was due to the existence of unemployment insurance. The implication that this information holds for the inflationary situation is that we may have to revise our notions of what level of unemployment is consonant with full employment. It also implies that the Federal Government's concern that the economy was not working at full capacity in 1971 – 72 when the

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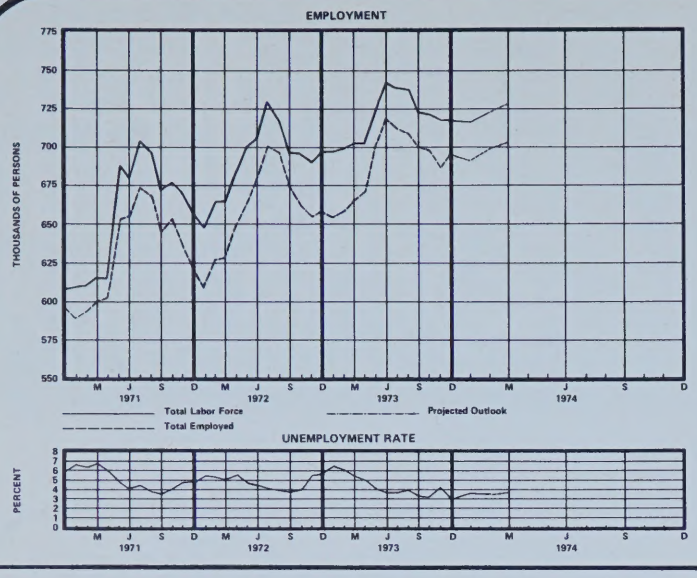
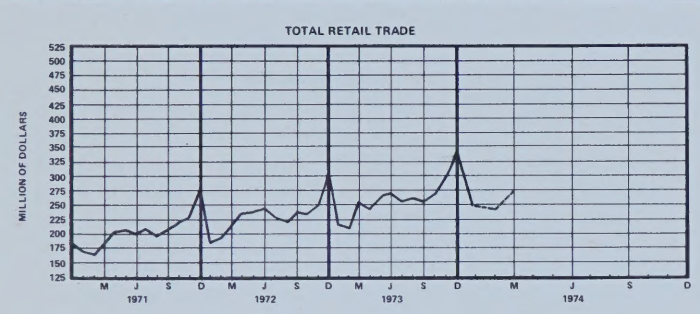
Alberta
INDUSTRY AND COMMERCE



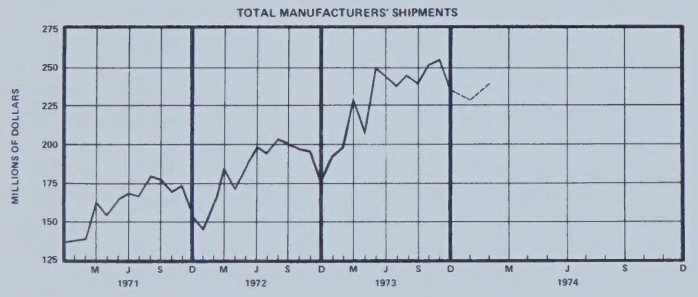
EMPLOYMENT

The unemployment rate in February 1974, was 3.5 percent a decrease of .1 percentage points from the previous month and 2.1 percentage points lower than February, 1973. The number employed increased by 8,000 in February and was 41,000 above the February 1973 level. The number of unemployed decreased by 1,000 in February and was 14,000 below the February, 1973 figure. For March, the labour force is expected to be approximately 730,000, with the total employed and unemployed at 703,000 and 27,000 respectively. April's outlook is for further seasonal declines in the number of unemployed, and increases in both the labour force and total employed.



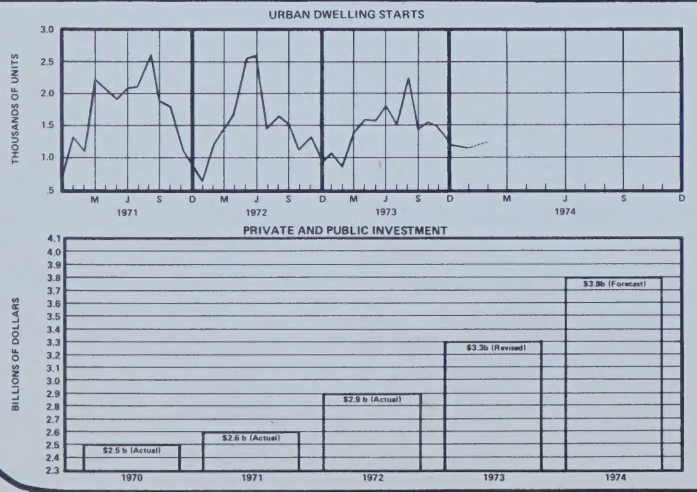
RETAIL TRADE

Retail trade in January was estimated at close to $249 million, an increase of 15 percent over January, 1973. On this basis, therefore, the February 1974 revised forecast for retail trade becomes $242 million, a 14 percent increase over the February 1973 figure. Prospects for March, 1974 indicate a value of approximately $272 million.



MANUFACTURING SHIPMENTS

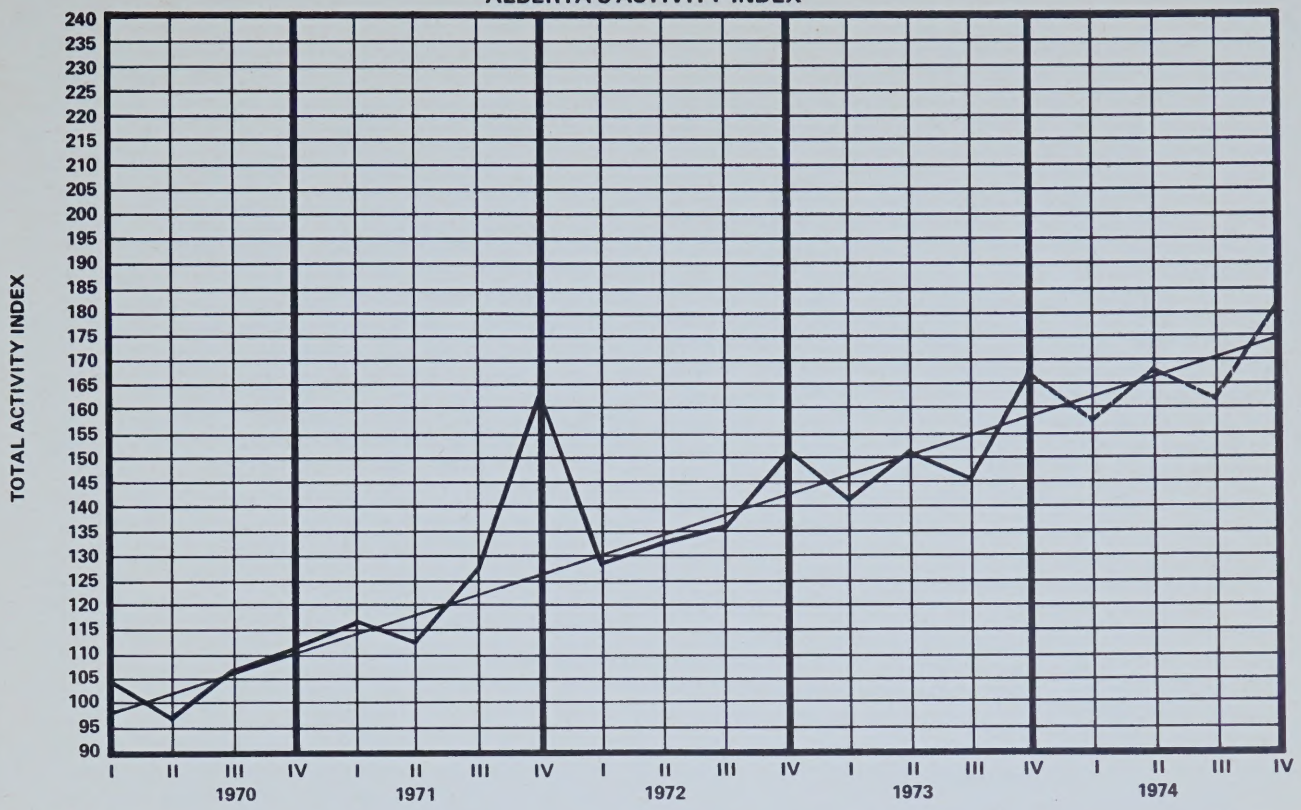
Revised estimates for the value of manufacturing shipments for 1973 place the total at nearly $2,794 million, a 20 percent increase over the 1972 level. On this basis therefore, the January revised forecast for manufacturing shipments becomes $228 million, a 15 percent increase over the January 1973 figure. Prospects for February, 1974 indicate a value of approximately $239 million.



HOUSING

Urban dwelling starts in January 1974, continued to reflect the upward trend which began last October. Since then, urban dwelling starts in Alberta have increased by almost 20 percent over the equivalent period one year ago. Starts in January 1974, totalled 1174, an increase of almost 10 percent from January, 1973. A revised forecast for February 1974, indicates about 1200 starts, with the total starts for the first quarter of 1974 expected to be approximately 3600. Based on these results, a major recovery in urban housing starts is possible for Alberta in 1974.

ALBERTA'S ACTIVITY INDEX



PERTINENT ECONOMIC INDICATORS FOR THE PROVINCE OF ALBERTA

INDICATOR	Percentage Change in Volume Activity Total Year 1971 - 1970	Total Year 1972 - 1971	Year to Date 1973 - 1972
MANUFACTURING			
Slaughtered Meat Production	+13.6	+ 3.3	- 2.2 (Jan. — Dec.)
Slaughtered Meat Exported	+12.6	+ 5.3	- 0.6 (Jan. — Dec.)
Refinery Production	+10.7	+21.4	+10.0 (Jan. — Dec.)
Cement Production	+ 4.5	+ 3.5	+ 7.8 (Jan. — Dec.)
MINING			
Oil Production	+ 9.4	+20.8	+19.6 (Jan. — Dec.)
Gas Production	+10.1	+16.8	+ 7.3 (Jan. — Dec.)
Footage Drilled	+ 1.8	+21.9	+28.3 (Jan. — Dec.)
Number of Wells Drilled	+ 9.6	+13.1	+33.2 (Jan. — Dec.)
Coal Production	+31.7	+14.1	+ 2.9 (Jan. — Dec.)
CONSTRUCTION			
Urban Dwelling Starts	+54.0	- 15.4	- 7.2 (Jan. — Dec.)
Rigid Insulation Board Shipments to Alberta	+15.6	+ 5.9	- 1.7 (Jan. — Dec.)
Value of Alberta Building Permits	+35.2	+12.1	+20.0 (Jan. — Dec.)
AGRICULTURE			
Grain Shipments	+ 8.8	- 2.9	- 16.4 (Jan. — Dec.)
Livestock Marketed	+15.1	- 1.6	- 6.4 (Jan. — Dec.)
Farm Cash Receipts	+ 9.8	+14.0	+32.3 (Jan. — Dec.)
FORESTRY			
Lumber Production	+ 6.1	+16.0	+33.6 (Jan. — Dec.)
Lumber Sales	+34.7	+ 5.7	+17.5 (Jan. — Dec.)
Lumber Exports	+26.5	+24.7	+ 2.5 (Jan. — Dec.)
Pulpwood Production	- 34.9	+47.8	+46.6 (Jan. — Dec.)

UNEMPLOYMENT RATE (Unadjusted)	FEBRUARY 1974	JANUARY 1974	FEBRUARY 1973	JANUARY 1973
Canada	6.8	6.9	7.3	7.7
Alberta	3.5	3.6	5.6	6.2
CONSUMER PRICE INDEX (1961 = 100)				
Calgary—Edmonton	149.1	147.8	137.6	137.1

unemployment rate was between 5½ and 6½ percent, was misplaced, and that the expansionary policies which were followed did not take up the slack in an unemployed economy but simply added another inflationary twist to an economy which was already full employed.

In the final analysis, therefore, it is reasonably clear that we were headed for a severe dose of "home-cooked inflation" in addition to the foreign variety which we have imported.

Inflationary expectations and wages

Moreover, people's inflationary expectations have been building up for such a long time and have received such a massive push since 1971–72 that it is going to be extremely difficult to regain control of domestic inflation. It should be apparent from the manner in which the size of wage rate increases held up during the 1969 recession and the eighteen month delay between the onset of accelerated inflation in 1972 and the demand for compensatory wage increases which emerged in the spring of 1973, that wage claims are going to provide plenty of fuel for inflation through 1975. Already, by the last quarter of 1973 one year contract average wage advances were at 10 percent, two year at 11.8 percent, compared with average gains of 7.9 percent and 8.1 percent in the same quarter of 1972. On this basis alone, therefore, little improvement in price performance can be expected.

Government policy

Government policy options are a savage deflation designed to kill inflation psychology at a blow, or a gradual easing down on government expenditure and the money supply. At the moment the Federal Government (and the U.S. Government) are opting for a gradual reduction of the money supply to a rate consistent with the growth rate of GNP at current prices. However, as Federal Reserve Board chairman, Arthur Burns acknowledges, this is a long term strategy, operating over a period of several years. We cannot expect short term relief from this direction.

Commodity prices. . .

For short term relief we can only turn to a hoped-for improvement on the international scene through an easing of world commodity prices and an appreciation of the Canadian dollar. With respect to world commodity prices a number of factors are involved. To begin with the growing recessions in Western Europe, Japan and the United States will lead to some easing of prices but it is unlikely that we will witness a collapse of commodity prices such as followed the Korean War boom. For one thing, that collapse was associated with a monetary stringency in the western consuming nations which is not present now or anticipated except in the case of Japan and the United Kingdom. For another the whole demand and supply balance for many basic commodities has changed. Rapidly growing living standards in developed and developing countries alike have brought an ever growing proportion of the world's population into income ranges where they can emulate North America's material and energy intensive style of living, and its agricultural resource devouring protein-rich diet. In addition the 25–30 age group, which constitutes the prime consumer of durable goods, is undergoing a dramatic expansion during the 1970's. In the U.S., for example, this group grew by 500,000 in the 1950's, and by 700,000 in the 1960's, but can be expected to grow by almost 50,000,000 during the 1970's. It seems unlikely in consequence that demand pressure on raw materials and food stuffs is going to decline substantially in the long term.

. . . and speculation

The main potential for short term relief from escalating commodity prices lies in a reduction in speculative purchasing. However the continuing gyration of currency markets can be expected to continue as the world sorts out its oil financing problems and that will ensure that commodities will remain a sure foundation in a shaking world which speculators will continue to rely upon as a refuge.

Upward float of the Canadian dollar

Appreciation of the Canadian dollar will help by reducing the price of imported goods in terms of Canadian currency, and, by making Canadian goods more expensive for foreigners, ease some of the pressure of demand on Canadian industry. However higher export prices will reflect on the domestic price level after an interval and it should also be remembered that the bulk of Canada's exports are on long contracts the prices on which are only adjusted after a considerable lag. The increases in commodity prices which occurred last summer, for example, may still be working their way through to the final Canadian export prices for the first three quarters of this year.

Conclusion

In the final analysis it's difficult to avoid the conclusion that the rate of inflation is more likely to accelerate than slow down in 1974. Any kind of return to the rates of price change which we experienced in the early and mid 1960's is a long way off. The continuation of high commodity prices and the undertaking of major resource projects such as the Arctic Gas pipeline, the James Bay project and the development of the Athabasca Tar Sands, will see to that.

BUSINESS OUTLOOK

Canada's Business Climate published by the **Toronto Dominion Bank** presents the following outlook for the Canadian economy during 1974.

— **Real GNP** is expected to grow by 4½ percent with **consumer prices** increasing by 7 percent as compared with the 7.6 percent recorded in 1973.

— **Consumer spending**, held back by slower sales of durable goods, will expand by just under 10 percent. **Consumer credit** is likely to rise by 10 to 12 percent. It is anticipated that **retail trade** will grow by approximately 10 percent led by sales of semi-durable and non-durable goods.

— **Business investment** has been forecast to increase by 21 percent but this figure may not be reached because of shortages in a wide variety of building materials and probable difficulties in obtaining imported machinery and equipment.

— **Housing starts** will be held back by more stringent credit restrictions and some shifts of recources to non-residential construction, to 250,000 or less. **Completions** are expected to reach 255,000 units but this will be insufficient to meet anticipated demand at current prices and incomes.

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